

Research Update:

Crelan S.A. Upgraded To 'A-' On Bail-In-Able Debt Buffer Constitution; Outlook Stable

September 19, 2023

Overview

- Crelan S.A. (Crelan) has so far issued €1.1 billion of senior nonpreferred debt (SNP) in 2023, adding to the €300 million already issued in September 2022 to comply with its minimum requirement for own funds and eligible liabilities (MREL) target.
- The development of subordinated additional loss-absorbing capacity (ALAC) is a source of protection for senior preferred creditors. We expect Crelan's ALAC buffer to stand at roughly 8.58% at end-2023 and remain sustainably above our 8% threshold for a second notch of ALAC uplift over the next two years.
- Therefore, we raised our long-term issuer credit ratings on Crelan and its core subsidiary Axa Bank Belgium (ABB) to 'A-' from 'BBB+'. We also affirmed our 'A-2' short-term ratings on the two banks.
- The stable outlook reflects our view that, over the next two years, the group will focus on integrating ABB with the aim to build a stronger, more efficient franchise while maintaining strong solvency and resilient asset-quality metrics.

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Rating Action

On Sept. 19, 2023, S&P Global Ratings raised its long-term issuer credit ratings on Crelan S.A. (Crelan) and Axa Bank Belgium (ABB) to 'A-' from 'BBB+'. We also affirmed our 'A-2' short-term issuer credit ratings on the two banks. The outlook is stable.

At the same time, we raised our long-term resolution counterparty rating on Crelan to 'A' from 'A-' and the short-term resolution counterparty rating to 'A-1' from 'A-2'.

Rationale

Crelan's senior creditors are increasingly supported by the building of its nonpreferred debt cushion. We think it is more likely that a resolution action on Crelan could ensure full and timely payment for senior preferred creditors as the bank continues to build its ALAC buffer. As of

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mid-September 2023, the bank issued a total of €1.4 billion SNP, which support its gone-concern buffer alongside its €209 million of subordinated Tier 2 debt.

We expect Crelan to have excess of roughly €100 million above our current 8% threshold for a second notch of ALAC uplift by year-end 2023. As Crelan has to comply with its MREL and subordination requirements and reach its €2 billion outstanding SNP target, we consider it highly likely the bank will carry out other issuances of SNP debt over the next two years, which we incorporate into our forecast. This supports our ALAC ratio being sustainably above the 8% threshold over the next several years and therefore led us to raise our ALAC support to two notches from one. This is because we see the current open bail-in resolution strategy--with the possibility of a transfer of business as a back-up--and significant bail-in-able debt as a positive for Crelan's senior bondholders.

We expect Crelan's net interest margin to peak in 2023. Despite the 5% profit decline at end-June 2023 compared to the same period in 2022, we acknowledge Crelan's first-half 2023 underlying performance has been strong, and we expect this trend to continue--although to a lesser extent--until year end. Crelan's hedging policy allowed it to fully benefit from rising interest rates in 2023, leading our measure of its annualized net interest margin (NIM) to reach 2% at first-half 2023, compared with 1.4% in 2022. The 65% increase of net interest income (NII) at the end of first-half 2023 is only marginally offset by lower fees, market-sensitive income, and higher cost of risk. We think the strong NII performance will carry over into the second half of the year, but the NIM should begin to weaken as most of the positive profit and loss effects from higher interest rates are booked in first-half 2023 and the pace of interest expense growth is set to increase quicker due to the gradual deposit shift to terms deposits.

Ultimately, the better-than-expected cost management led us to slightly revise our cost-to-income forecast to 71%-75% for 2023 from 73%-81%. However, our cost-to-income forecast over 2024-2025 remains the highest of the peer group by a significant margin, partly due to the ABB integration.

Over the longer term, Crelan's 'bbb' stand-alone credit profile could be supported by delivering on the legal merger with ABB, the full integration of ABB's IT systems, and subsequent business synergies while navigating the risks entailed by such a large acquisition.

Belgium's recently issued bonds do not affect our view on Crelan's resilient liquidity. In September 2023, the Belgian government proposed "bons d'Etats" to its population. Thanks to an interesting gross rate of 3.3% and advantageous fiscal treatment, Belgian residents bought roughly €22 billion of this issuance, which therefore lowered Belgian banks' deposit bases and liquidity positions. Crelan disclosed that it sold €1.2 billion of "bons d'Etats" through its networks. We expect a similar depletion in the bank's core deposit base, which grew by 2% to €43.2 billion at first-half 2023. We estimate this will impair Crelan's loans to deposits (LTD) ratio by about three percentage points, increasing it to 115%. Despite Crelan having the highest LTD ratio among its peer group since ABB's integration (due to ABB's covered bond refinancing model), we do not see this as a weakness in our view on the bank's liquidity and funding profile. We calculate Crelan's adjusted LTD ratio--including its covered bonds stock and incorporating the deposit depletion of €1.2 billion--of around 91%, which is in line with our adequate liquidity and funding assessment.

Outlook

The stable outlook reflects our view that, over next two years, the group will focus on integrating ABB with the aim to build a stronger, more efficient franchise while maintaining strong solvency and resilient asset-quality metrics.

While we see a positive element from ABB's integration, as it could create a retail group with greater scale in the concentrated domestic market, we think the process poses challenges, notably blending corporate cultures, large branch networks, and IT systems, while enhancing digital capabilities. As a result, we think synergies and profitability improvements could be gradual.

Downside scenario

Although unlikely as this stage, we could lower our ratings if the integration of ABB poses substantial operating or business challenges that prevent the bank from profitability turnaround.

Upside scenario

We are unlikely to revise Crelan's 'bbb' stand-alone credit profile upward and so raise the ratings over the next two years. But we could consider this if Crelan successfully integrates ABB, realizes material synergies, and aligns its profitability and efficiency metrics more closely with those of higher-rated peers.

Ratings Score Snapshot

	To	From
Issuer Credit Rating	A-/Stable/A-2	BBB+/Stable/A-2
SACP	bbb	bbb
Anchor	a-	a-
Business position	Constrained (-2)	Constrained (-2)
Capital and earnings	Strong (+1)	Strong (+1)
Risk position	Moderate (-1)	Moderate (-1)
Funding and liquidity	Adequate and adequate (0)	Adequate and adequate (0)
Comparable ratings analysis	0	0
Support	+2	+1
ALAC support	+2	+1
GRE support	0	0
Group support	0	0
Sovereign support	0	0
Additional factors	0	0
AXA Bank Belgium	To	From
Issuer Credit Rating	A-/Stable/A-2	BBB+/Stable/A-2

SACP--Stand-alone credit profile.

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Crelan S.A., Feb. 27, 2023
- Crelan S.A. 'BBB+/A-2' Ratings Affirmed Amid Axa Bank Belgium Integration; Outlook Stable, Nov. 30, 2022

Ratings List

Upgraded

	To	From
Crelan S.A.		
AXA Bank Belgium		
Issuer Credit Rating	A-/Stable/A-2	BBB+/Stable/A-2

Upgraded

	To	From
Crelan S.A.		
Resolution Counterparty Rating	A/--/A-1	A/--/A-2

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceid/504352>. Complete ratings

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